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In the Supreme Court of the United States

OCTOBER TERM, 1964

No. 356

THE ACRO MANUFACTURING COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 74a-88a)[1] are reported at 39 T.C. 377. The opinion of the Court of Appeals (Pet. 11-17) is reported at 334 F. 2d 40.

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[1] "R." references are to the appendix to petitioner's brief in the Court of Appeals. In the remainder of this brief petitioner will be referred to as the taxpayer.

JURISDICTION

The judgment of the Court of Appeals was entered on July 8, 1964. (Pet. 18.) The petition for a writ of certiorari was filed on August 7, 1964. The jurisdiction of this Court is invoked under 28 U.S.C. 1254 (1).

QUESTION PRESENTED

Whether the courts below correctly held that assets distributed to the taxpayer corporation on the complete liquidation of its wholly-owned subsidiary, and then immediately sold by the taxpayer, were capital assets in the hands of the taxpayer, the sale thus resulting in a capital loss.

STATUTE INVOLVED

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 1221. CAPITAL ASSET DEFINED.

For the purposes of this subtitle, the term "capital asset" means property held by the taxpayer (whether or not connected with his trade or business), but does not include—

(1) stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business;

(2) property, used in his trade or business, of a character which is subject to the allowance for depreciation provided in sec-

tion 167, or real property used in his trade or business;

* * * *

(4) accounts or notes receivable acquired in the ordinary course of trade or business for services rendered or from the sale of property described in paragraph (1); * * *

* * * *

STATEMENT

During the years in question Acro Manufacturing Company, the taxpayer, was engaged in the business of manufacturing and selling precision switches and thermostatic controls. On December 9, 1954, it acquired the outstanding capital stock of Universal Button Company, a corporation engaged in the business of manufacturing metal buttons for work clothes. In March, 1955, the taxpayer began negotiations with Talon, Inc., for the disposition of this investment. The taxpayer's representatives were unwilling to sell the Button stock as such, because they feared undesirable tax consequences. Finally, however, the taxpayer and Talon entered into an agreement calling for the complete liquidation of Button and the sale by taxpayer of the Button operating assets, subject to Button's business liabilities. Button was completely liquidated on June 30, 1955, and taxpayer, upon receipt of the operating assets, immediately transferred them to Talon in accordance with the terms of their agreement. (R. 10a-35a, 75a-77a; Pet. 11-12.)

The Tax Court, in a reviewed opinion, held that the sale by taxpayer of the assets in question resulted in a capital loss. (R. 80a-88a.) The court of appeals affirmed. (Pet. 11-18.)

ARGUMENT

Section 1221 of the Internal Revenue Code of 1954, *supra*, pp. 2-3, defines a capital asset as "property held by the taxpayer" with certain specified exceptions. These include inventory, real propery and depreciable property used in the business, and accounts and notes receivable acquired in the ordinary course of business for services rendered or from the sale of inventory. In the hands of Universal Button Company, the assets in question qualified as noncapital within those exceptions. But it does not follow that they retained the same character when transferred to the taxpayer. By the express terms of the statute, the character of the property as capital or noncapital assets is determined by its relationship to the taxpayer's business, not to the business of the transferor.

Taxpayer, engaged in the business of manufacturing precision switches and thermostatic controls, never entered into the business of manufacturing and selling metal buttons for work clothes. Those items which represented inventory to Button were not related to the product manufactured and sold by taxpayer in its business. The accounts receivable were not acquired by taxpayer from the sale of its stock in trade or its services in the ordinary course of carrying on its business. The real estate and depreciable

property were never used in its trade or business. The taxpayer chose to liquidate its investment in the Button corporation, and it did so by dissolving Button and immediately selling off these assets. The assets thus were capital assets in taxpayer's hands, and the loss to it from the sale is a capital loss.

That taxpayer received the assets in a complete liquidation—to which Section 332 of the Internal Revenue Code of 1954 (26 U.S.C. 1958 ed., Sec. 332) is applicable—should not change this result, as the courts below held. The cited provision, which allows the complete liquidation of a subsidiary into its parent to proceed without the immediate recognition of gain or loss by the parent, represents an attempt by Congress to encourage the simplification of corporate structures. *Commissioner* v. *Phipps*, 336 U.S. 410, 421; *Helvering* v. *Credit Alliance Co.*, 316 U.S. 107, 112. It does not, however, presuppose that the noncapital nature of distributed assets carries over to the parent.

The taxpayer argues that the holding below creates opportunities for manipulation (Pet. 4-5), but, here, it is the taxpayer which attempts to change the character of its loss from the disposition of its investment in the Button corporation.

The holding in this case is an application of the cardinal principle of tax law that the business of a corporation is separate and apart from the business of its shareholders. *National Carbide Corp.* v. *Commissioner*, 336 U.S. 422; *Interstate Transit Lines* v. *Commissioner*, 319 U.S. 590; *Moline Properties* v. *Commissioner*, 319 U.S. 436; *Burnet* v. *Common-*

wealth Imp. Co., 287 U.S. 415. See, also, *Whipple* v. *Commissioner*, 373 U.S. 193; *New Colonial Co.* v. *Helvering*, 292 U.S. 435; 7 Mertens, *Law of Income Taxation* (Rev.), Sec. 38.05. There is no conflict, and there is no other basis for review by this Court.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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